

BOARD OF EQUALIZATION

In the Matter of the Petition for
Redetermination of State and Local
Use Tax;

X-----

Petitioner

DECISION AND RECOMMENDATION

No. X-----

The above-entitled matter came on regularly for hearing on Tuesday October 5, 1976, in Pasadena, California. Robert H. Anderson, Hearing Officer.

Appearing for Petitioner: X-----

X-----

Appearing for the Board: Mr. Roy Huey, Auditor
Pasadena District Office

Protest

Pursuant to an audit covering the period from 10-01-72 through 09-30-75, and a determination issued on February 10, 1976, petitioner protests the assessment of use tax on an item purchased ex tax which the auditor labeled "tooling". The measure of the tax is \$30,214.

Contentions

Petitioner's representative contends that the product they purchase from outside vendors is a form of typography and is exempt from tax.

Summary

Petitioner is a corporation engaged in business as typographer that uses both the cold type and photo composition methods. There was a prior audit ending with the third quarter of 1972.

The product involved in petitioner's purchases may be punched cards, perforated tapes or magnetic tapes which when run through petitioner's computer equipment produces copies of the original manuscript or document.

Petitioner does typography through the use of computers as well as through the use of the more established methods. Where computer typography is used the original document, a manuscript for example, is first put into computer language. This is on punched cards, perforated tape or magnetic tape.

The tape is run through a computer which produces another tape. This tape is run through a photocomposing machine which makes the page of printed matter that started out in the form of a manuscript. The page of printed matter is delivered to the customer as a reproduction proof.

Because of petitioner's volume of business, some of the work has to be turned over to other firms to do. One type of outside work is putting the manuscript into computer language on tapes or cards.

Petitioner purchased tapes containing manuscripts in computer language, and these purchases are the subject to this controversy. Petitioner issued resale certificates on some of the purchases from California vendors; other purchases were from out-of-state vendors. In either case, use tax has been assessed on the purchase price of the tapes on the ground that they are a form of "tooling" or manufacturing aids used to make what is ultimately the reproduction proof.

Following is a summary of the steps involved:

1. Manuscript put in computer language on tape. (This is purchased by petitioner from outside sources.)
2. Tape with computer language is run through computer which produces another tape (tape 2).
3. Tape 2 is run through a photocomposing machine which produces a page of printed matter that started out in the form of a manuscript.
4. The page of printed matter is delivered to the customer as the end product sold by petitioner; it is used as a reproduction proof.

Conclusions

Regulation 1541 (Printing and Related Arts) contains the following guidelines with respect to the application of tax to "Composed Type".

1. The composition of type, whether text type or display type, is the performance of a service, and tax does not apply to charges for such service, unless the service is

part of the sale of printed matter in which case tax applies to the gross receipts from the sale of the printed matter without any deduction for typography. Typographers are the consumers of materials such as foundry type, typesetting machinery, metal forms, galleys, proofing paper, ink, film, and cleaners used in the performance of their service.

2. Hot Metal Composition. Tax does not apply to the composing of type, whether the type is set by hand or by type composing machine, even though the typographer may transfer composed metal type to his customer. Further, tax does not apply to composition even though the typographer may transfer galley proofs to his customer, or may transfer reproduction proofs of composed type in lieu of the composed metal type.

Note: The term reproduction proof includes a direct impression of composed type forms containing type matter only, provided the impression is to be used exclusively for reproduction.

3. Cold Type Composition (Including Phototypesetting and Computer Typesetting). Tax does not apply to the composing of type regardless of whether the type is composed by means of such simplified cold type methods as standard typewriter, Varsity or Justowriter, by means of photolettering or headlining machines, or by means of a photocomposition (including computer photocomposition) method.

Note: Tax does not apply to the transfer of the direct product of the type composition service containing type matter only (whether paper or film) or a direct copy (on paper or film) of the product, provided the product is to be used exclusively for reproduction.

The pages, in type form, that petitioner sells to the customers are used by the customers as "reproduction proofs" and as such are not subject to tax. If they were photocopied and transferred in the form of negatives or positives to be used as reproduction proofs (for reproduction purposes), they would still not be subject to tax under the regulation.

As an analogy, a person could take a manuscript and use a type composing machine and come up with composed metal type which he sells to petitioner. Under the regulation, the sale of the composed type, transferred to petitioner, would not be subject to tax.

Petitioner then could take that composed type and run off a galley proof and a reproduction proof and transfer only the galley proof and the reproduction proof to his customer in lieu of the composed type. Under such circumstances, the sale of the reproduction proof and galley proof would not be subject to tax under the regulation if the reproduction proof was used exclusively for reproduction.

At first blush it would appear that petitioner's purchase of the manuscript language on tape in computer language form is analogous to the purchase of the same manuscript language in "composed type" form and it probably is.

However, the authority for exempting the composed type in Regulation 1541 is found under section 6010.3, which provides:

"Sale" and "purchase", for the purposes of this part, do not include (a) the fabrication or transfer by a typographer of composed type or reproduction proofs thereof for use in the preparation of printed matter or (b) the fabrication or transfer of such reproduction proofs or impressed mats when the fabrication is for, and the transfer is to, a printer or publisher for use in printing. (Underline added.)

The foregoing is a tax exemption statute which the courts have said must be strictly construed against taxpayers claiming exemptions. Luer Packing Co. v. State Board of Equalization (1950) 101 Cal. App. 2d 99; Good Humor Co. v. State Board of Equalization (1957) 152 Cal. App. 2d 879; Santa Fe Transportation Co. v. State Board of Equalization (1959) 51 Cal. 2d 531.

Accordingly, the statutory exemption is limited to "composed type" and reproduction proofs produced thereof. The computer tape is not "composed type" within the meaning of that word. In strictly construing the exemption statute, the Board has interpreted "composed type" to mean only that which is readable to the naked eye as distinguished from that which is only readable with the use of a machine. The invisible electronic changes on the tape that produces a printed page or which is used to produce a second tape that is used to produce the printed page is readable to the naked eye is not "type".

The printed page, readable to the naked eye that is produced from the computer tape is analogous to the printed page produced, with a typewriter, Varsity or Justowriter and the application of tax to the printed page produced with the tape is the same as that which is produced by the typewriter, Varsity or Justowriter, this is the "photocomposition" referred to as "computer photocomposition" in the regulation.

It is reasonable to assume that the use of computers to produce printed pages including reproduction proofs may not have been contemplated by the Legislature when section 6010.3 was enacted, otherwise the exemption would have expressly included the method. Be that as it may, the requirement of strict construction of the exemption statutes precludes broadening it by a regulation that treats a computer tape in the same way as "composed type".

Recommendation

Redetermine without adjustment to the protested item.

Robert H. Anderson, Hearing Officer

12/23/76